INDUSTRIAL
CUSTOMERS OF
NORTHWEST
UTILITIES

KEN CANON
EXECUTIVE DIRECTOR

December 13, 2002

Mr. Tony Usibelli
Director, Energy Policy Division
Department of Community, Trade
and Economic Development
PO Box 43173
Olympia, WA 98504-3173

RE: Comments of Industrial Customers of Northwest Utilities (ICNU) on the Washington State Energy Strategy Update

Dear Tony,

Industrial Customers of Northwest Utilities (ICNU) represents large industrial customers purchasing electric power from Washington's publicly-owned and investor-owned utilities. Most of these industrial customers produce commodity products and all face intense global competition. For that and other reasons, it is unfortunate that the Advisory Committee did not have an industrial representative throughout this process.

Historically, Washington's low-cost electricity provided a competitive advantage that offset higher transportation and other costs. That is no longer the case. In fact, many Washington industrial customers face electrical costs much higher than internal and external competitors. With Washington suffering high unemployment and significant economic challenges, it is disappointing that this key point seems to be notably absent in the November 25, 2002, draft.

The other issue that could use more exploration is the necessity to balance long-term costs versus near-term rate impacts. For example, integrated resource plans typically examine costs over a 20-year period. These costs include resources that have 20 - 40 year lives. Different resources have different financial characteristics. Some are more capital intensive, while others are more fuel intensive. Resources also have different impacts on near-term rates. Focusing only on long-term costs and discounting those costs over decades can ignore significant near-term rate impacts. For businesses facing a weak economy, critical competitive challenges and other large electrical users such as the state of Washington itself, these near-term rate impacts should not be ignored. There needs to be a balance and that balance may need to change over time.

Following are comments on specific Guiding Principles:

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**Guiding Principle #1**

Adopting integrated resource plans (IRPs) does not ensure adequate resources. IRPs are only plans, it takes actions to ensure that resources are acquired. We would assume that most large electric utilities in Washington had IRPs during the recent energy crisis.

The narrative of this Guideline is confusing. While it is expected that traditional utilities will continue to serve customers, does the narrative imply that Washington would prohibit a utility from offering retail access to certain customers? After all, Washington currently has a number of industrial customers on the market and that PSE program is considered to be one of the best market access programs in the nation. We are also uncertain whether "acquire the resources" in the second bullet includes market purchases in addition to hard assets.

**Guiding Principle #3**

With BPA's wholesale rates now at 32 mills/kWh and perhaps going higher, what benefits are to be protected? Shouldn't the state be focused on recapturing the "historic" (23 m/kWh power) benefits of the BPA system?

**Guiding Principle #4**

A cost-based system, through overbuilding, can provide reliable power, few supply shortages, little price volatility - and sustained high prices. To add real value, a cost-based system should strive to produce low cost power. While everyone focuses on the high prices that resulted from market manipulation, most overlook the low prices that prevailed through the last half of the 1990s. They also overlook the reliability issues, price volatility, shortages, and steep price increases that occurred under the cost-based system in the 1970s.

This guideline suffers from a lack of clarity, compounded by the narrative. For example, the last sentence in the second paragraph says that "Washington continues to be extremely cautious about increasing our reliance on market forces to provide our electricity supply." What does this mean? Is it focused on retail or wholesale? It could mean that Washington is taking a position that it does not want utilities to purchase power on the wholesale market. It could mean that Washington does not want to rely on IPPs to develop new generating resources, but to instead have utilities rate base all new resources. It could mean that it does not want any large customer to have market access - even if those customers may be larger than many Washington utilities. A strategy is only beneficial if it has sufficient clarity to clearly illuminate a preferred course of action. This guideline does not.

It would be worthwhile to devote part of the narrative to discuss what is needed to the extent that the utility system does rely on the wholesale market and market forces generally. This includes clear responsibility for risks, demand response and other contingency programs, and good market oversight.

**<u>Guideline #6</u>**

How does a state foster a predictable and stable investment climate? Would this Principle have a different meaning if it were revised to read, "Foster a predictable and stable investment climate to facilitate adequate and efficient access to capital markets for all Washington businesses." What is the state prepared to do for the utility sector that they wouldn't be prepared to do for all other Washington industries? While we agree with the second and third bullets, we are very concerned about the meaning of the first bullet. How would public officials reassure capital markets? Would it be through higher ROEs, pre-approval of resources, or faster regulatory approvals? We would recommend deleting the first bullet, or if it is retained, to add another bullet that would highlight the requirement for prudent utility management decisions and a thorough and fair rate-setting process.

Sincerely,

/s/

Ken Canon